REACTION

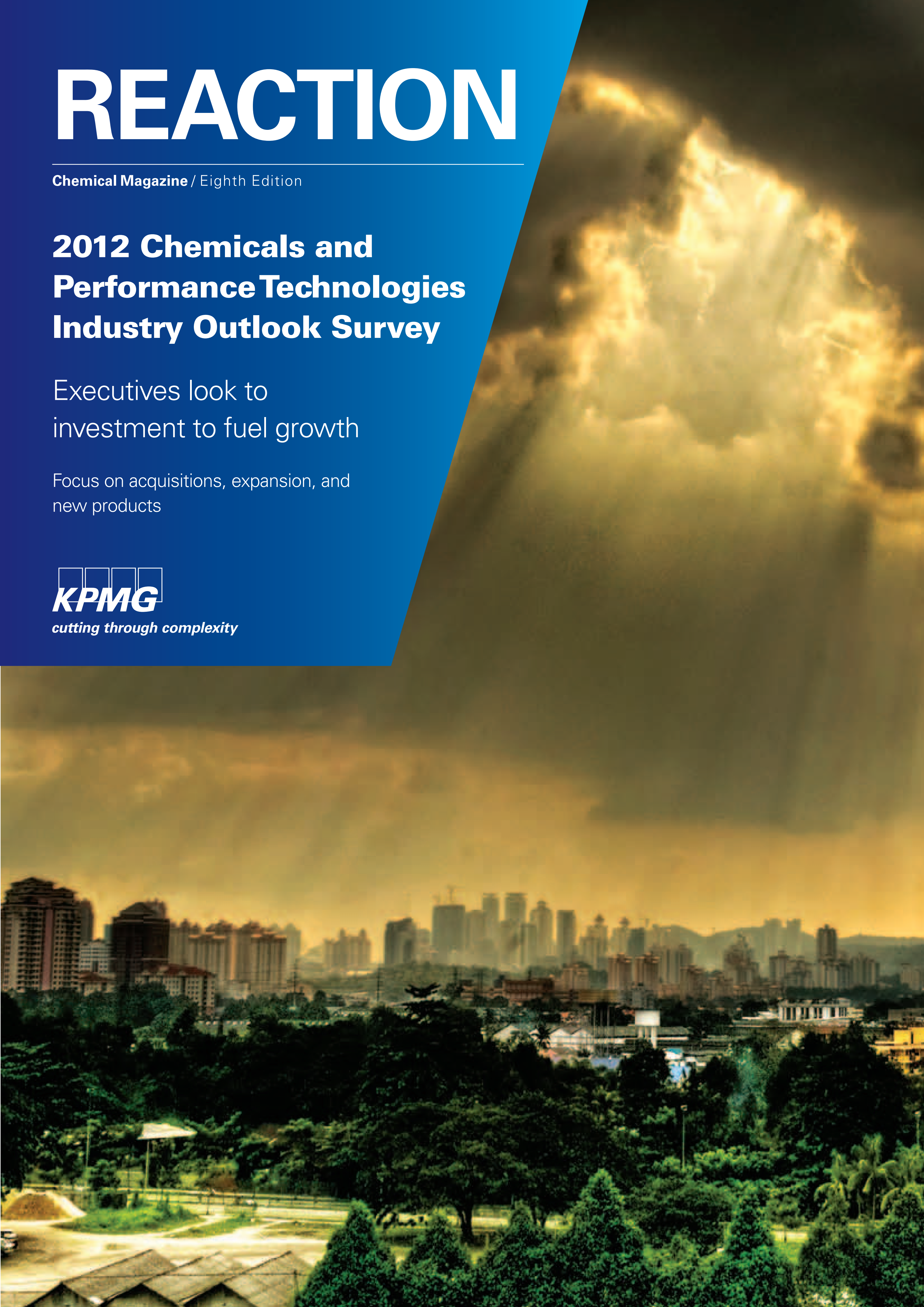
Chemical Magazine / Eighth Edition

2012 Chemicals and Performance Technologies Industry Outlook Survey

Executives look to investment to fuel growth

Focus on acquisitions, expansion, and new products

KPMG
cutting through complexity



KPMG's Business Pulse Survey

KPMG in the UK, the Audit, Tax and Advisory firm, surveyed top-level executives in the global chemicals and performance technologies industry during the third quarter of 2012. Participants were asked about business conditions in their sector, drivers of revenue growth, investment trends and factors that may impede or support their sector's recovery.

TABLE OF CONTENTS

Introduction

Welcome to a special edition of Reaction, in which KPMG International takes an in-depth look at the global chemicals and performance technologies industry by focusing on the results of KPMG's 2012 Industry Outlook Survey. This annual survey polls chemicals industry executives from the US, Europe, and the Asia Pacific region. The survey covers the industry outlook for business conditions, M&A, capital spending, revenue, headcount and other key categories across the three regions.

Perhaps unsurprisingly, the macroeconomic environment is much more of a concern for executives than it was in the 2011 survey – with executives in Europe and the US seemingly more worried than their counterparts in Asia. This comes through strongly in the revenue and hiring expectations for the next twelve months which are much less bullish than they were 12 months ago.

Despite those concerns, however, companies generally continue to focus on growth and expansion. Strong financial discipline since the last downturn has enabled companies to generate significant cash reserves and many executives report that they are actively seeking to deploy those reserves to pursue strategic acquisitions and new product development in order to access long-term growth.

On behalf of KPMG International, I would like to thank those executives who participated in this survey. I hope the findings are useful to you in addressing market challenges and opportunities. I also welcome the chance to discuss this study and its implications for your business in the year ahead.

Mike Shannon
Global Leader for Chemicals and Performance Technologies

Key findings from

KPMG's 2012 Chemical Industry Pulse Survey

The KPMG survey was conducted in July 2012 and reflects the responses of 156 senior executives in the Chemical industry – 53 in the US, 50 in Europe, and 53 in Asia-Pacific. Based on revenue in the most recent fiscal year, 21 percent of respondents work for institutions with annual revenues exceeding USD10 billion, 35 percent with annual revenues in the USD1 billion to USD10 billion range, and 44 percent with revenues in the USD100 million to USD1 billion range.

Key findings from the survey include the following:

- Seventy-two percent of industry executives indicate that their companies have significant cash on the balance sheet and 51 percent say their companies' cash positions have improved from last year.
- Nearly two thirds (63 percent) of all executives plan to increase capital spending over the next year. For the second year in a row, Asian executives were most bullish about capital spending with 81 percent expecting an increase, versus 48 percent in the US and 58 percent in Europe.
- Worldwide, the highest priority investment areas are new products or services (35 percent), and the acquisition of a business (33 percent). US executives indicate that they plan to be much more aggressive investing in these two areas than their Asia-Pacific and European counterparts.
- A large majority (90 percent) of executives indicate that their companies are likely to be involved in a merger or acquisition in the next two years – up from 83 percent last year. US executives were most optimistic about being buyers (48 percent); European respondents were the most likely sellers (52 percent).
- Despite plans for expansion, the macroeconomic environment is far more of a worry for executives than this time last year. For instance, 80 percent of chemical executives expect revenue to increase next year, a drop from the 85 percent in 2011, who expressed higher revenue expectations. Meanwhile, 65 percent of respondents say that headcount will increase next year, a decline from 71 percent who had higher hopes last year.

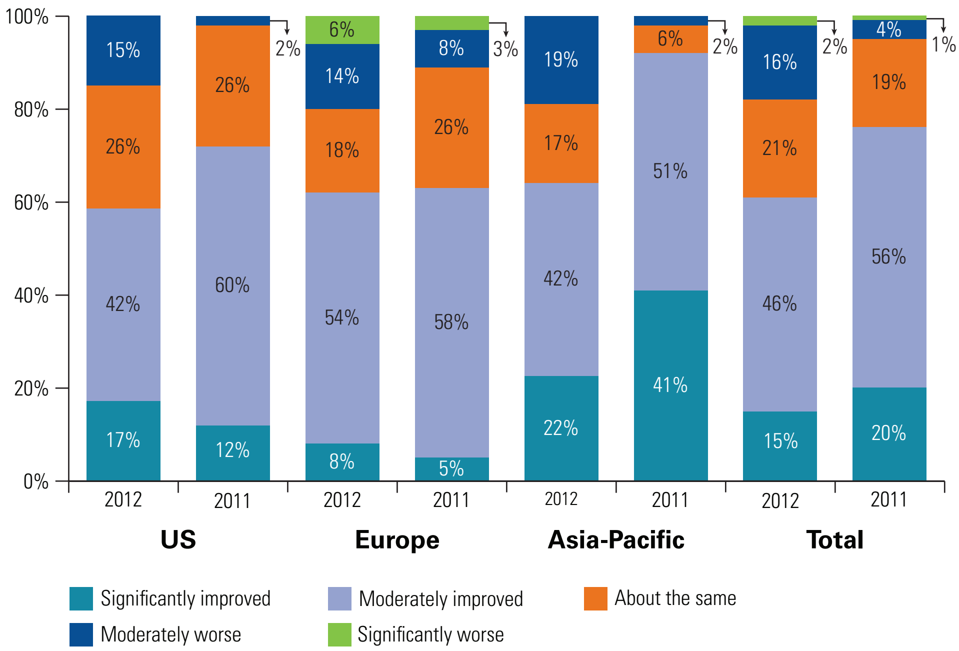
Nearly **three-quarters of chemicals industry** executives say their **company plans** to increase **capital spending** over the next year.

Economic **environment**

Modest expectations for economy

Forty-five percent of respondents worldwide stated that the global economy would improve moderately in 2013. Surprisingly, the greatest optimism was in Europe, with 54 percent of the respondents looking forward to a moderate improvement.

A year from now, what are your expectations for the economy?

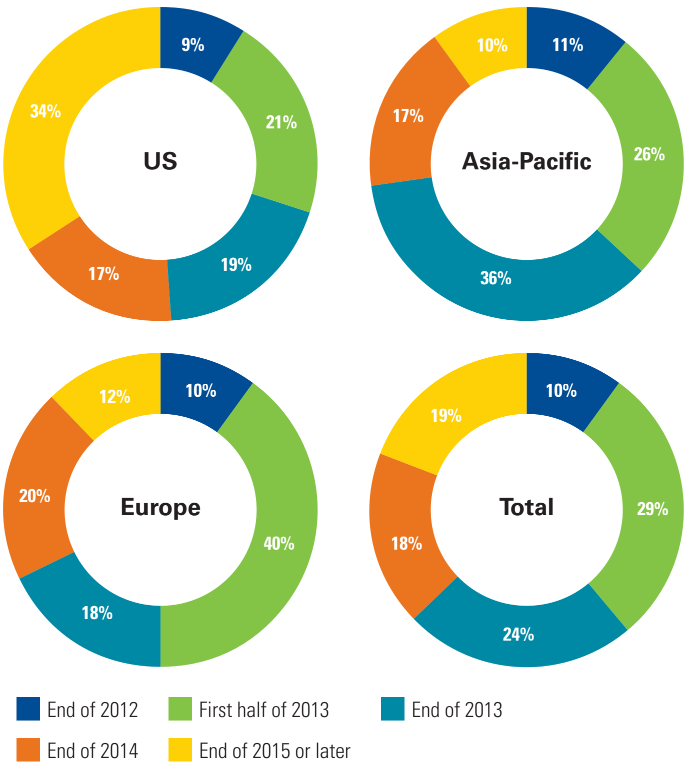


Source: KPMG International 2012

Full recovery expected later than before

Compared to last year, respondents were generally less optimistic about the recovery of the economy. In 2011, 26 percent felt that the economy would recover by the end of the next year (2012), whereas only 10 percent of this year's respondents expected recovery by 2013. In the same way, predictions of a substantial recovery within two years have also declined, from 42 percent in 2011 to only 18 percent in 2012.

When do you think the global economy as a whole will recover? Recovery will be substantially complete by what year?

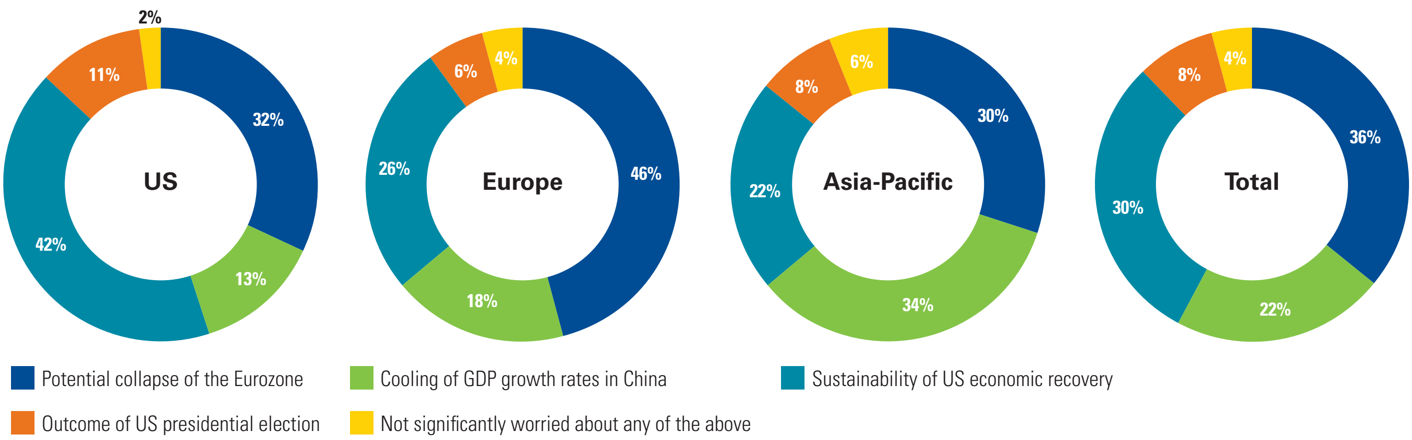


Source: KPMG International 2012

Collapse of the Eurozone a key concern

The potential collapse of the Eurozone as well as the sustainability of the US economic recovery were the greatest areas of concern for the majority of respondents. Issues such as the outcome of the US presidential election were seen as less problematic.

Which of the following gives you the greatest cause for concern?



Source: KPMG International 2012

Sector outlook

Estimated revenue growth

Most respondents anticipate growth rates between 6 to 10 percent. European respondents were relatively optimistic, with a total of 72 percent expecting increases of up to 10 percent.

What do you estimate your company's revenue growth rate will be over the next year?

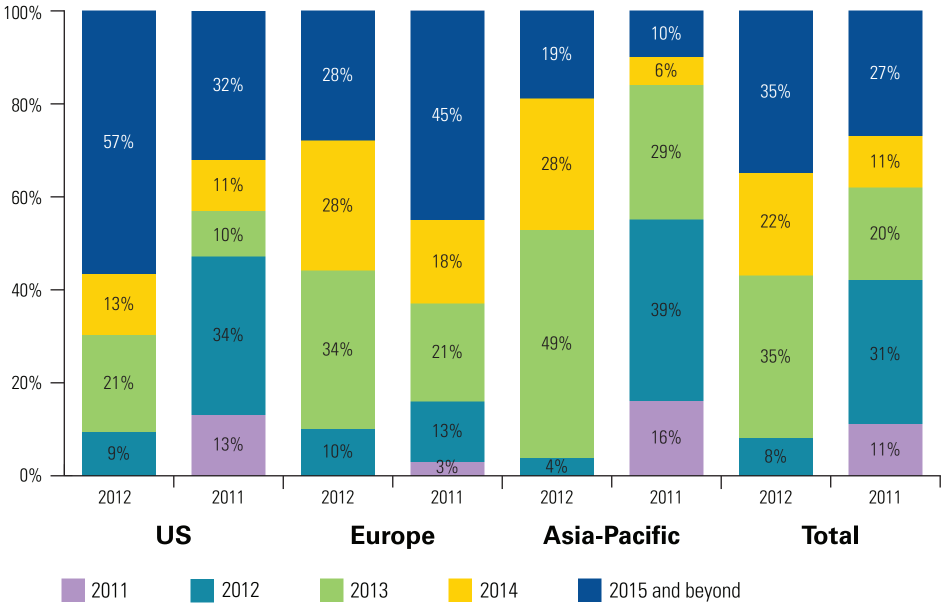
	US	Europe	Asia-Pacific	Total
Increase by more than 20%	04%	02%	02%	03%
Increase by 11% to 20%	13%	00%	17%	10%
Increase by 6% to 10%	34%	32%	40%	35%
Increase by 1% to 5%	34%	40%	23%	32%
No impact/change	06%	16%	07%	10%
Decrease by 1% to 5%	06%	02%	07%	05%
Decrease by 6% to 10%	03%	02%	00%	02%
Decrease by 11% to 20%	00%	04%	02%	02%
Decrease by more than 20%	00%	02%	02%	01%

Source: KPMG International 2012

Projections for greatest sales volumes

Most executives looked to 2013 or 2014 for a peak in sales volume. This finding can be compared with responses to the earlier question about economic recovery. In both cases, US executives were on average more pessimistic, with many expecting that a return to previous performance levels would take three or more years.

In what year do you predict sales volume to be at its greatest for your company?

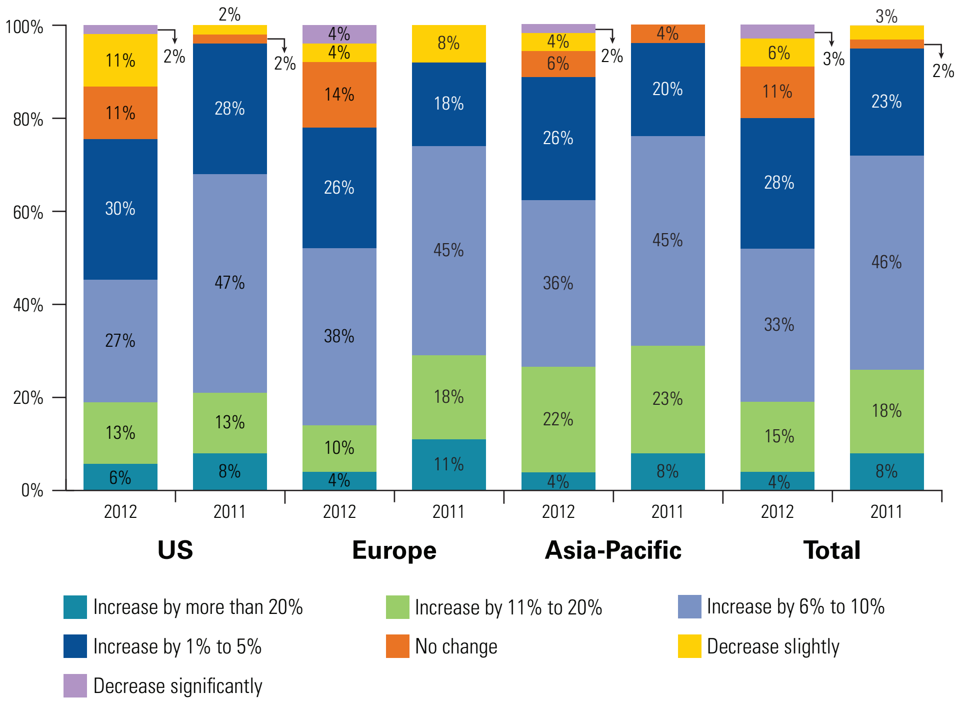


Source: KPMG International 2012

Raw material costs

Significant cost increases for raw materials were indicated by the majority of respondents across all regions. The largest number indicated an increase of between 6 and 10 percent.

What do you anticipate will happen to your company's raw material costs over the next year?



Source: KPMG International 2012

Barriers to growth

Energy prices and lack of customer demand were cited most frequently by executives as the top growth barriers in the industry. Additionally, nearly a third (32 percent) of respondents in the US cited pricing pressures, versus 15 percent of respondents in Asia-Pacific and 8 percent in Europe.

Which of the following are the most significant growth barriers facing your company over the next year?

Multiple responses allowed. Number of responses shown.

	US	Europe	Asia-Pacific	Total
Lack of qualified workforce	08	04	06	18
Access to and managing capital	08	08	05	21
Energy prices	13	16	21	50
Increased taxation	08	06	09	23
U.S. dollar strength	06	10	16	32
Lack of customer demand	11	14	09	34
Regulatory and legislative pressures	10	06	03	19
Risk management issues	05	07	08	20
Staying on top of emerging technologies	07	02	04	13
Foreign competition	05	05	03	13
Labor costs	04	06	09	19
Pricing pressures	17	04	08	29
Inflation	02	08	05	15
Volatile commodity/input prices	13	04	04	21
Exchange rate fluctuations	03	02	04	09
Other	00	00	00	00

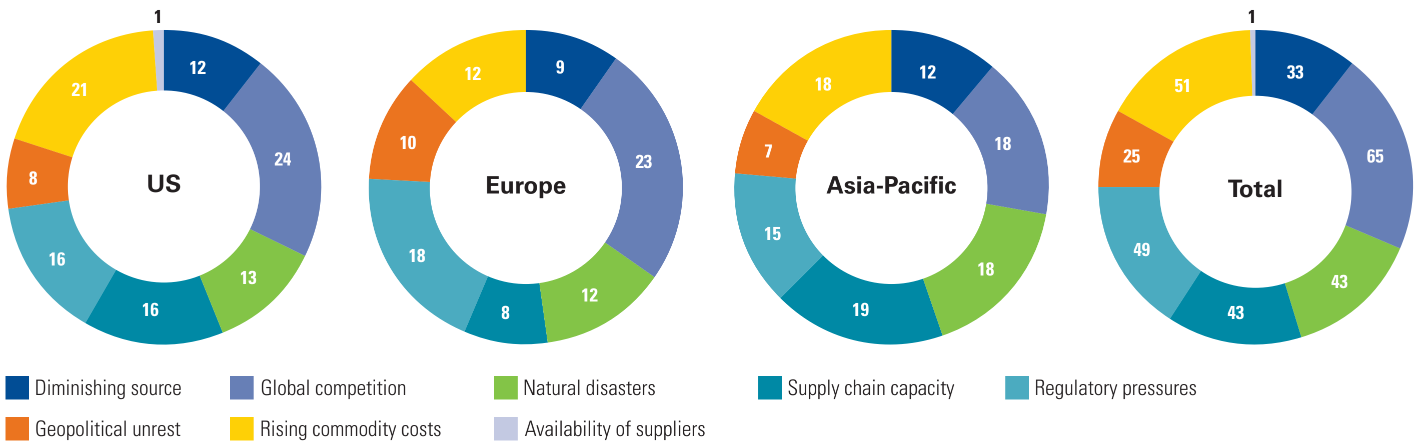
Source: KPMG International 2012

Supply chain stability

For global chemical companies, global competition is the greatest threat to supply chain stability, according to respondents. Rising commodity costs were also a concern, outpacing even regulatory pressures.

What are the biggest risks to your supply chain stability?

Multiple responses allowed. Number of responses shown.



Source: KPMG International 2012

Current headcount

Almost half of the respondents (47 percent) stated that their companies had increased headcount by more than 4 percent. Only 15 percent reported no change.

Compared with this time last year, how would you describe your company's current headcount?

	US	Europe	Asia-Pacific	Total
Increased by more than 10%	09%	04%	11%	08%
Increased by 7% to 10%	11%	22%	26%	20%
Increased by 4% to 6%	17%	18%	23%	19%
Increased by 1% to 3%	15%	18%	13%	15%
About the same	19%	18%	08%	15%
Decreased by 1% to 3%	15%	08%	11%	13%
Decreased by 4% to 6%	04%	06%	02%	04%
Decreased by 7% to 10%	04%	06%	04%	04%
Decreased by more than 10%	02%	00%	02%	01%
Not sure/don't know	04%	00%	00%	01%

Source: KPMG International 2012

Expectations for hiring

The majority of respondents indicated an increase in their company's headcount of up to 10 percent in the coming year. At the same time, almost a fifth did not anticipate any hiring; while in the US 21 percent actually expect to decrease headcount in the coming year.

How do you expect your company's headcount to change one year from now?

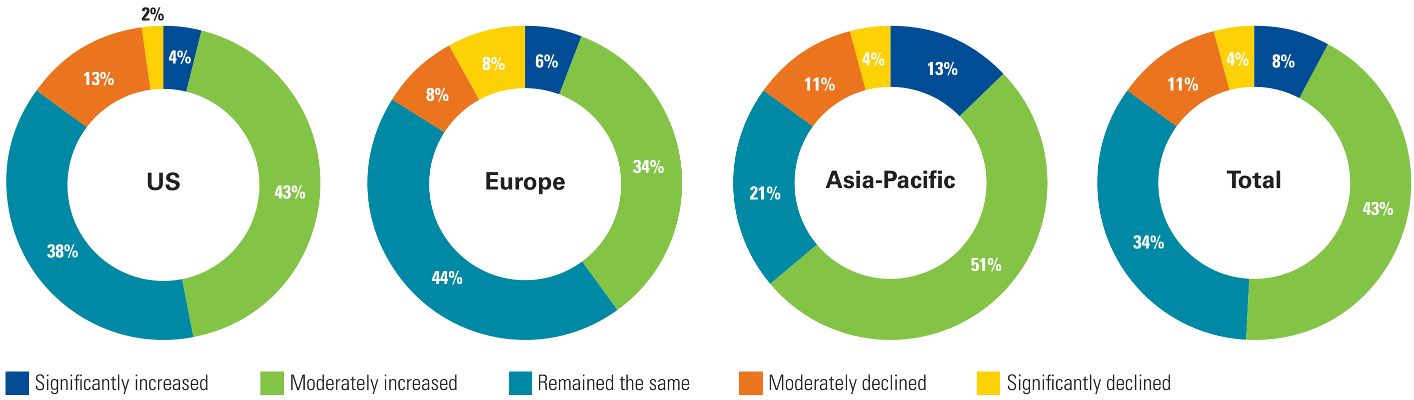
	US	Europe	Asia-Pacific	Total
Increase by more than 10%	08%	00%	09%	06%
Increase by 7% to 10%	09%	12%	28%	17%
Increase by 4% to 6%	13%	34%	17%	21%
Increase by 1% to 3%	26%	12%	23%	21%
About the same	21%	24%	13%	19%
Decrease by 1% to 3%	09%	08%	04%	07%
Decrease by 4% to 6%	06%	04%	02%	03%
Decrease by 7% to 10%	02%	04%	02%	03%
Decrease by more than 10%	04%	02%	00%	02%
Not sure/don't know	02%	00%	02%	01%

Source: KPMG International 2012

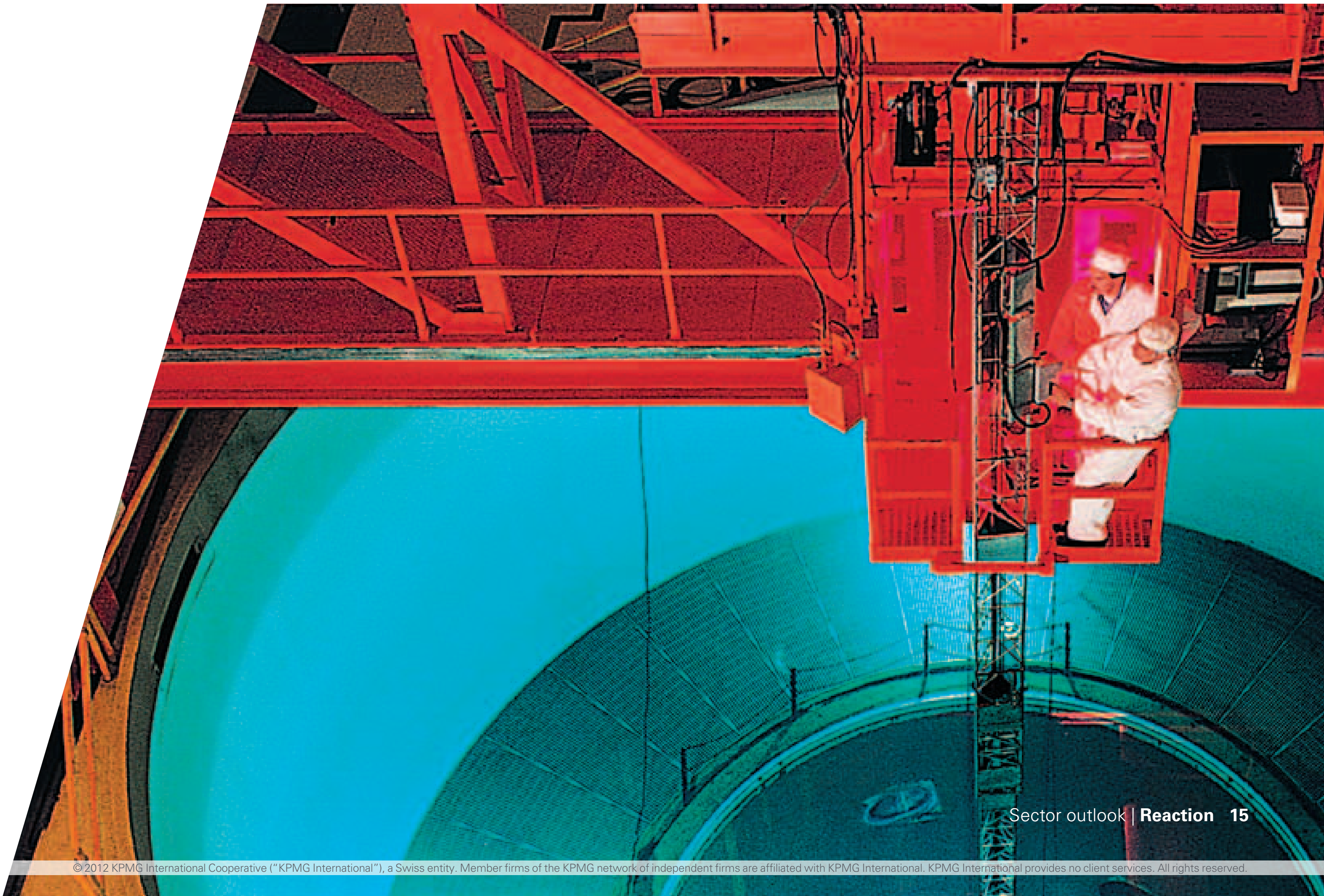
Cash positions

Most respondents stated that their company's cash position had remained the same or had moderately increased since 2011. However, respondents indicating significant increases were fewer in number than respondents indicating moderate or significant declines.

Compared to a year ago, your company's cash position (cash on balance sheet) has:



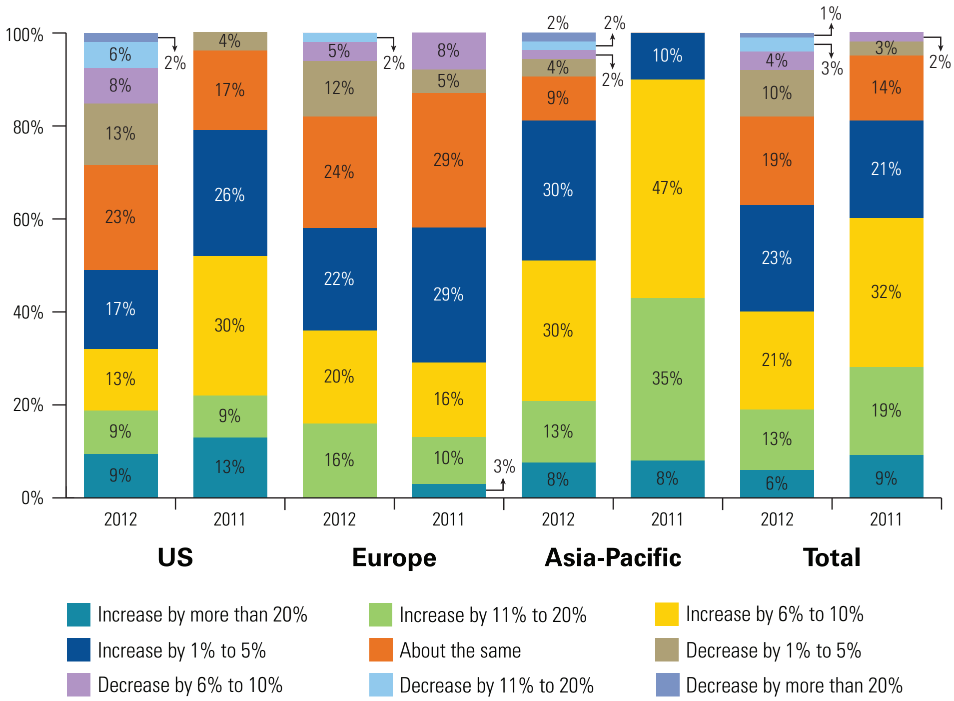
Source: KPMG International 2012



Capital spending and investing

On the whole, most respondents indicated a cautious approach to capital spending in the coming year. Over 20 percent plan on a 1 to 5 percent increase. Nearly an equal number predicted a 6 to 10 percent increase. An additional 19 percent of those surveyed expected to keep their spending about the same.

What is the outlook for capital spending by your company over the next year?



Source: KPMG International 2012

Future **focus areas**

Greatest focus of management

Compared to other respondents, executives from chemicals companies in the US indicate a greater focus on significant cost reductions as well as investments in organic growth from new product development, pricing strategies and geographic expansion than their global counterparts.

What is the top initiative from a management perspective for the next two years in terms of energy, time, and resources?

	US	Europe	Asia-Pacific	Total
Merger/acquisition	10%	10%	02%	08%
Strategic divestiture of current assets	09%	06%	15%	10%
Navigating significant changes in the regulatory environment	04%	06%	13%	08%
Significant changes in business model	17%	26%	19%	21%
Significant improvement of operation processes and related technology	08%	22%	23%	17%
Significant changes to financial processes and related technology	02%	16%	09%	09%
Significant cost reduction initiatives	23%	10%	13%	15%
Significant investment in organic growth (new product development, pricing strategies, geographic expansion)	23%	04%	04%	10%
Improve enterprise risk management programs/processes	04%	00%	02%	02%

Source: KPMG International 2012

"Balancing **potential** global economic risks with the need to expand into **new products** and markets to capture **growth** will be **key to success.**"

Paul Harnick, Global COO for Chemicals and Performance Technologies

Spending in key areas

Interestingly, when it comes to key areas in which executives are willing to spend, responses varied significantly based on region. Almost twice as many US executives than Asia-Pacific executives cited acquisition of a business or new products and services as one of three areas for increased spending. However, this ratio was reversed for the two regions when it came to spending on information technology.

In which three areas do you expect your company to increase spending the most over the next year?

Multiple responses allowed. Number of responses shown.

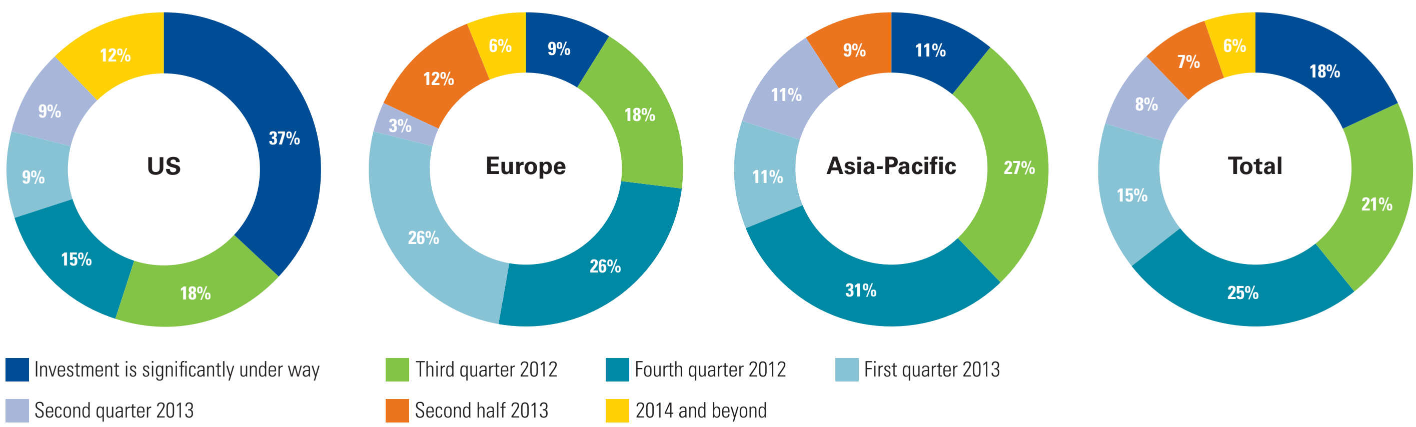
	US	Europe	Asia-Pacific	Total
New products or services	22	18	14	54
Acquisition of a business	24	16	12	52
Geographic expansion	09	18	15	42
Expanding facilities	18	09	13	40
Information technology	10	13	22	45
Business model transformation	07	10	09	26
Research and development	14	11	09	34
Advertising and marketing	05	06	08	19
Green/sustainability initiatives	09	04	12	25
Employee compensation and training	05	06	08	19
Regulation/control environment	05	02	04	11
Other	01	00	00	01

Source: KPMG International 2012

Investment timeframe

Almost 40 percent of US respondents reported that investment is significantly underway, almost doubling the results reported from this region in 2011. Thirty-one percent of Asia-Pacific respondents believe investing will heat up in the fourth quarter of this year. Meanwhile, more than half (52 percent) of European respondents said that they anticipate investments to occur during the fourth quarter of 2012 or first quarter of 2013.

What do you think is the most likely time frame for investment?



Source: KPMG International 2012

M&A and NPD to drive **revenue growth**

Gearing up for investment and growth

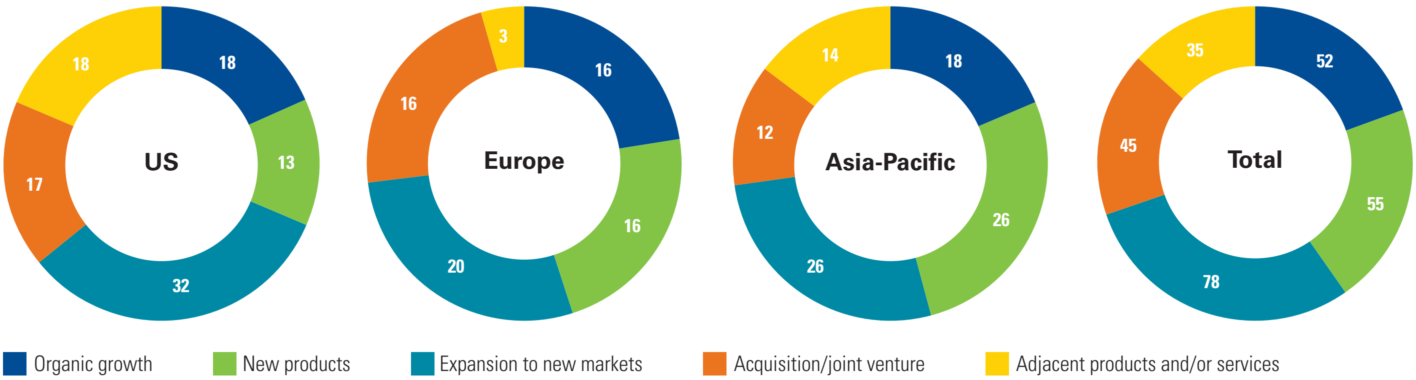
Despite escalating costs, rigorous competition and a struggling global economy, most global chemical industry executives say they will use a significant amount of cash on their balance sheets to spur growth, mainly through acquisitions and new product development. This optimism is strongest in emerging economies. At the same time, most respondents are less optimistic about growth in revenue, especially as compared to a year ago.

Driving revenue growth

Key drivers included expansion to new markets and new products. Organic growth ranked somewhat below new products and somewhat ahead of acquisitions or joint ventures.

What do you think will be the biggest drivers of your company's revenue growth over the next one to three years?

Multiple responses allowed. Number of responses shown.



Source: KPMG International 2012

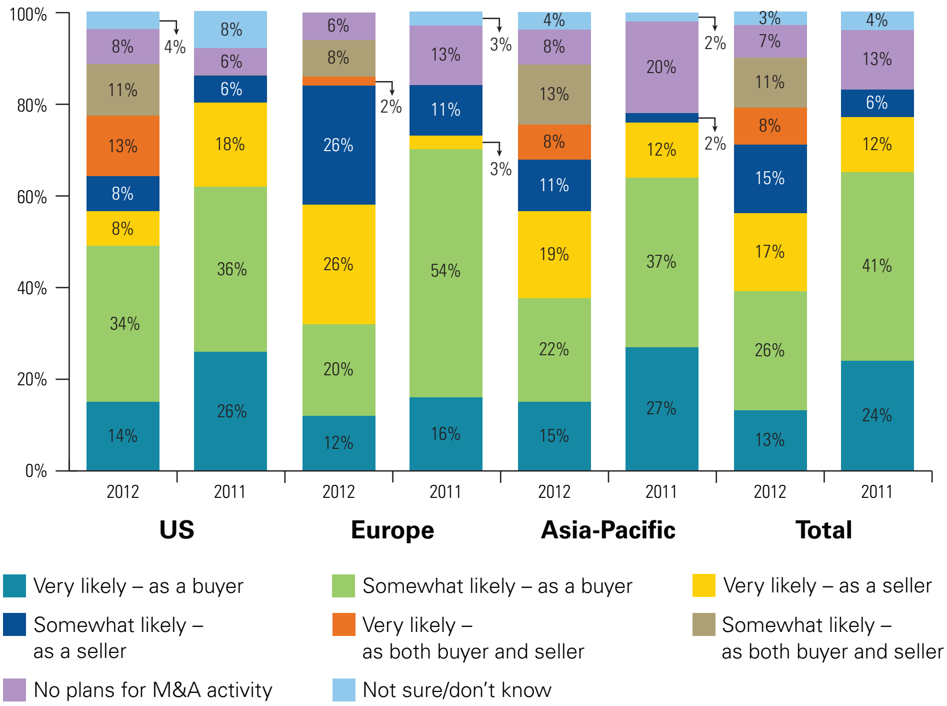
"Despite economic headwinds, the **chemicals sector** has experienced some **positive momentum** in the past year. The **improved cash positions** will allow them to be more aggressive to drive **growth and innovation.**"

Mike Shannon, Global Chair, Chemicals and Performance Technologies

M&A activity still climbing

Ninety percent of executives indicate that their companies are likely to be involved in a merger or acquisition in the next two years – up from 62 percent in the 2011 survey. Notably, respondents in the US were the most focused on being buyers while European respondents were the most likely sellers.

What is the likelihood that your firm will be involved in a merger/acquisition in the next two years?



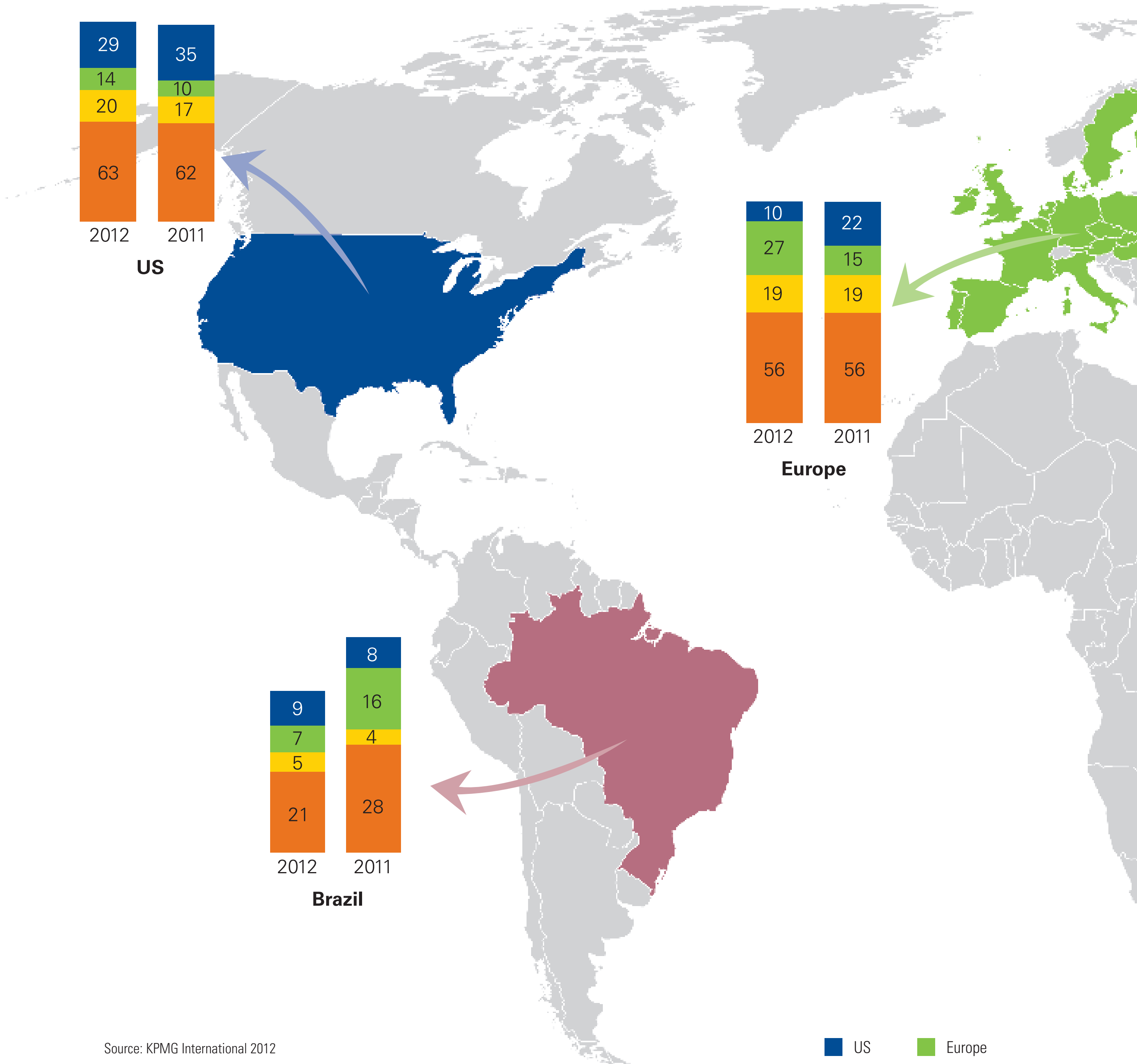
Source: KPMG International 2012

Investments by region

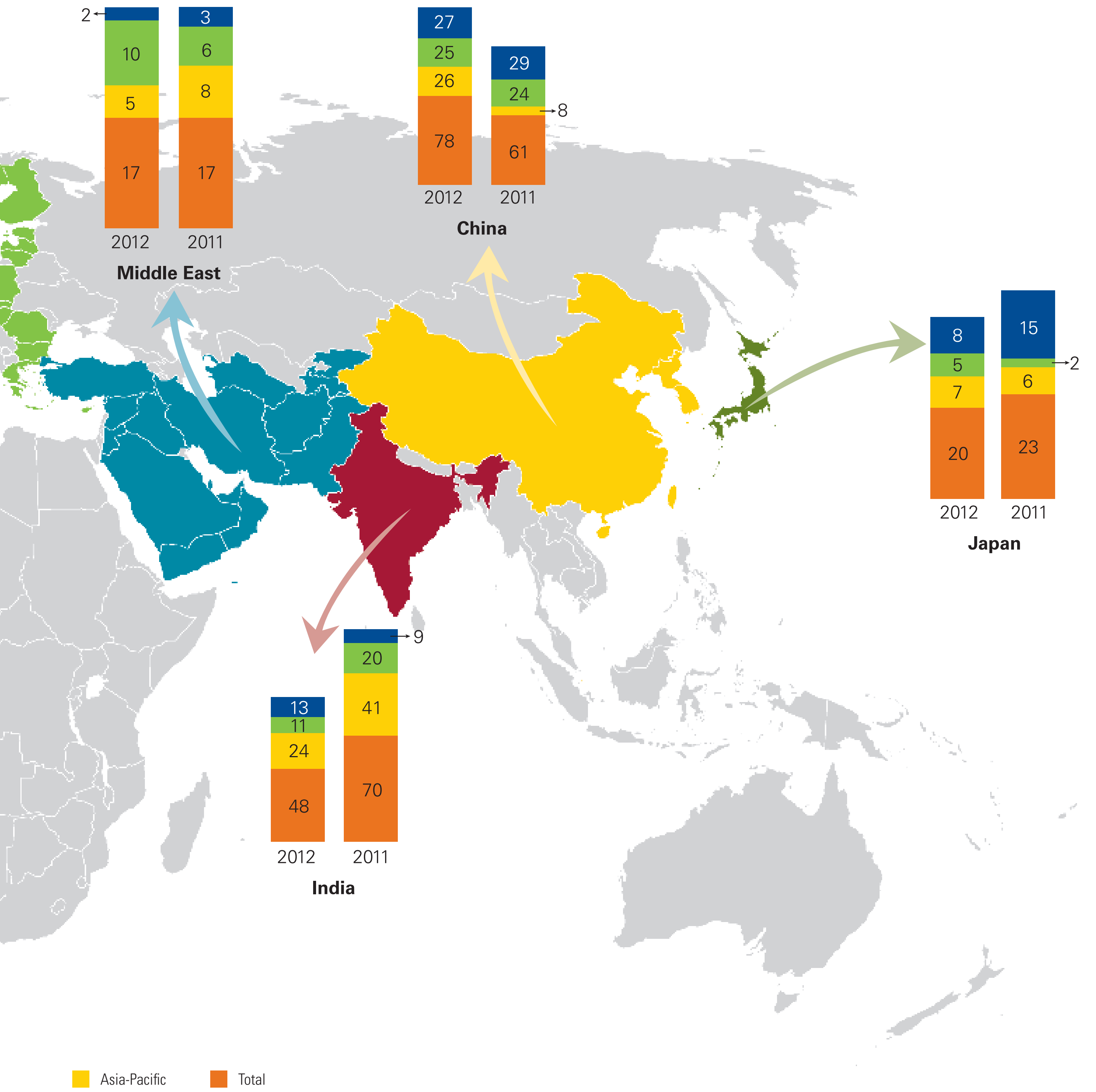
Respondents named China, the US, and Europe as the geographic regions that will be the focus of investment. US and European executives showed a much stronger preference for domestic investment. China remained a favored investment location for executives in all three regions.

Which geographical region(s) will be the focus for the majority of your investment capital over the next two years?

Multiple responses allowed. Number of responses shown.



Source: KPMG International 2012

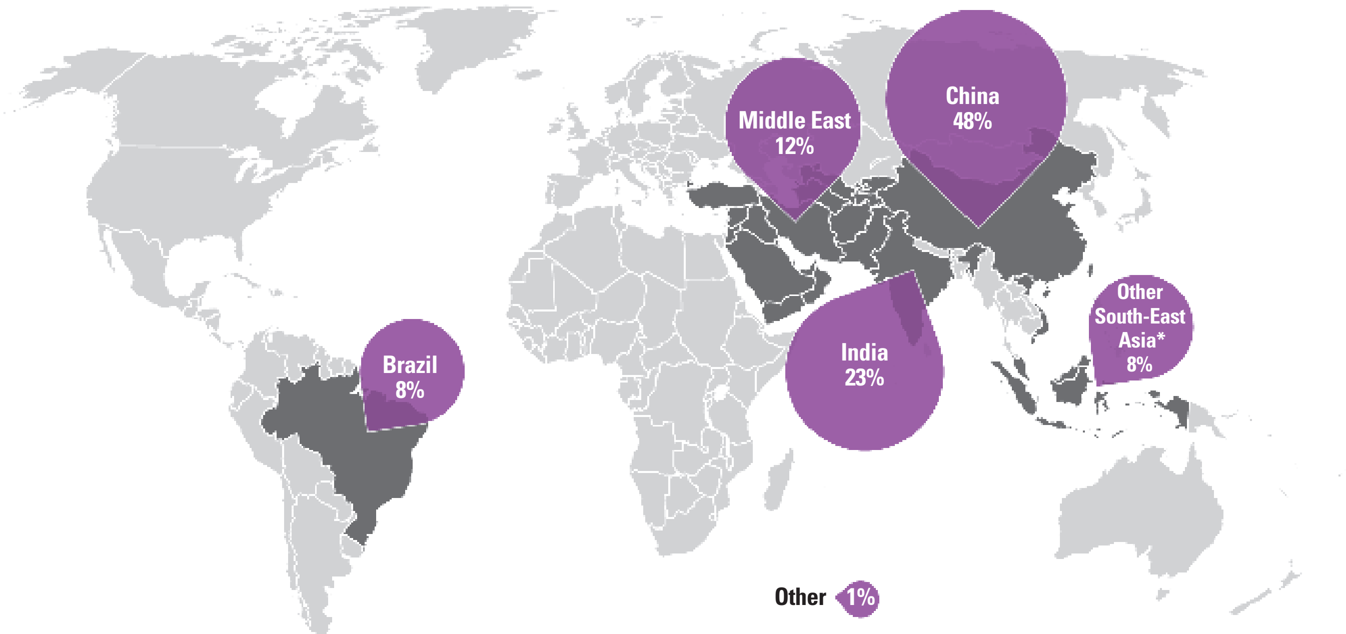


Middle East
2012: 2, 10, 5, 17
2011: 3, 6, 8, 17
China
2012: 27, 25, 26, 78
2011: 29, 24, 8, 61
Japan
2012: 8, 5, 7, 20
2011: 15, 2, 6, 23
India
2012: 13, 11, 24, 48
2011: 9, 20, 41, 70
Asia-Pacific
Total

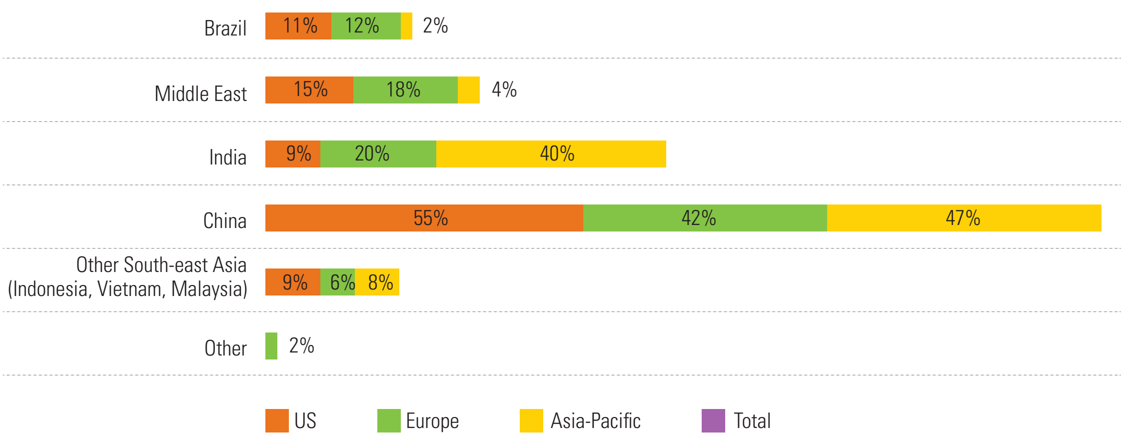
Emerging-market growth by region

As expected, China and India were cited as the two greatest areas for market growth. However, the Middle East placed ahead of Brazil, perhaps reflecting recent weak economic performance of the Brazilian economy combined with strength of the Real.

Where do you expect to see the highest rates of emerging market growth in the chemical industry over the next five years?



*Indonesia, Vietnam, Malaysia

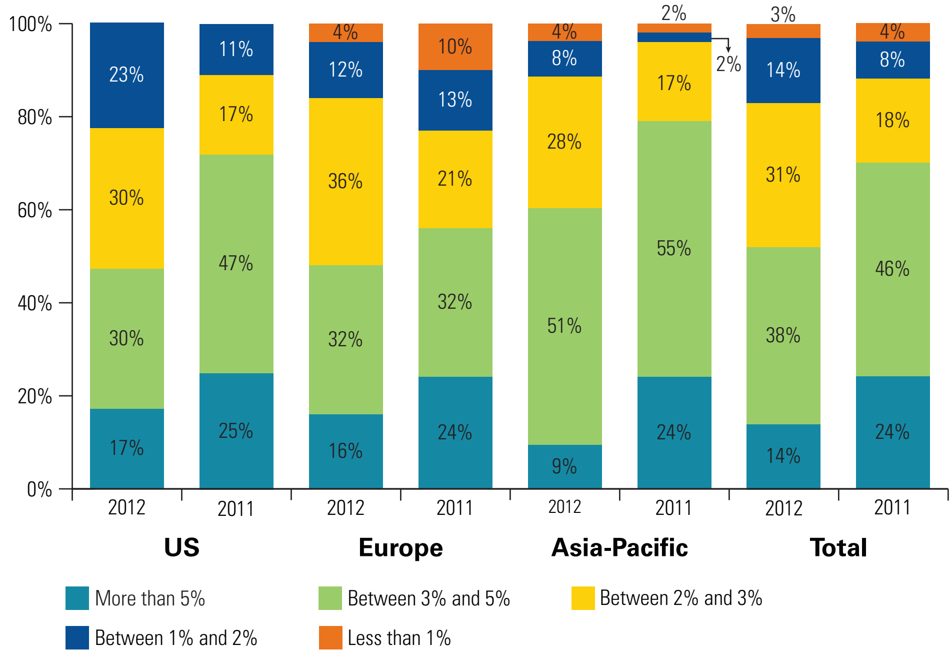


Source: KPMG International 2012

R&D investments

Most respondents indicated that their companies would be investing between 2 and 3 percent of revenues in R&D. Slightly more than half of Asia-Pacific executives expected R&D investments of between 3 and 5 percent.

What proportion of revenue do you expect to invest in R&D over the next twelve months?



Source: KPMG International 2012

Conclusion

Following the return to growth in 2010 and 2011, the chemicals and performance technologies industry in 2012 is being affected by the ongoing global macroeconomic concerns – Eurozone debt issues, doubts about the sustainability of the US economic recovery and cooling of emerging market growth rates. This is reflected in the survey results, which at the macro level are much more pessimistic than 12 months ago.

Despite this, the majority of chemical executives have continued to focus on cost and cash discipline, such that many companies have significant cash reserves. Companies are also undertaking or planning significant changes in business models, improvements in operational process and technology, investments in organic growth from new product development as well as growth strategies focused on geographic expansion.

While the executives this year were less optimistic about revenue and hiring compared to 2011, 80 percent expect revenue to increase next year, and 65 percent say that their headcount will increase – both indicators of a growing and well-managed industry.

KPMG:
Serving the Global Chemical Industry

KPMG's Global Chemicals & Performance Technologies practice is one of the leading advisers to the industry worldwide. KPMG member firms audit more of the companies on the Chemical Week Billion Dollar Club List than any other professional services organization and provide multi-disciplinary tax and advisory services to a majority of the other Billion Dollar Club companies. These services are backed by a global network of dedicated industry professionals, experienced in working together on large cross-border assignments in many chemical producing regions of the globe. Furthermore, KPMG member firms are committed to supporting the global Chemicals & Performance Technologies industries over the long term. From our sponsorship of chemical CEO round tables worldwide, to member firms' participation in industry events at local, regional and global levels, we are dedicated to playing an active role in the operation of the global chemical industry.

Contacts

Global Head of Chemicals and Performance Technologies
Mike Shannon
Tel: +1 973 912 6312
e-mail: mshannon@kpmg.com

In Asia
Norbert Meyring
KPMG in China
Tel: +86 (21) 6288 2298
e-mail: norbert.meyring@kpmg.com.cn

In Australia
Steve Tonner
KPMG in Australia
Tel: +61 (3) 9288 5377
e-mail: stonner@kpmg.com.au

In Canada
Robert Jolicoeur
KPMG in Canada
Tel: +1 416 777 3733
e-mail: bjolicoeur@kpmg.ca

In France
Wilfrid Lauriano do Rego
KPMG S.A.
Tel: +33 1 55 68 68 72
e-mail: wlaurianodorego@kpmg.com

In Germany
Vir Lakshman
KPMG AG
Wirtschaftsprufungsgesellschaft
Tel: +49 211 475 6666
e-mail: vlakshman@kpmg.com

In India
Vikram Hosangady
KPMG in India
Tel: +91 44 3914 5101
e-mail: vhosangady@in.kpmg.com

In Italy and KSA
Johan Bode
KPMG Al Fozhan & Al Sadhan
Tel: +966 874 8500
e-mail: jcbode@kpmg.com

In Japan
Arihiro Yanagisawa
KPMG in Japan
Tel: +81 35218 6704
e-mail: arihiro.yanagisawa@jp.kpmg.com

In Netherlands
Lex Gardien
KPMG N.V.
Tel: +31 (0)10 453 4163
e-mail: gardien.lex@kpmg.nl

In South America
Anselmo Macedo
KPMG in Brazil
Tel: +55 11 2183 3152
e-mail: amacedo@kpmg.com.br

In Switzerland
Erik Willems
KPMG AG
Tel: +41 44 249 45 20
e-mail: ewillems@kpmg.com

In UK
Andrew Monro
KPMG in the UK
Tel: +44 20 73111698
e-mail: andrew.monro@kpmg.co.uk

Global Tax Lead
Frank Mattei
Tel: +1 267 256 1910
e-mail: fmattei@kpmg.com

Global Marketing
Ashley Lewis
Tel: +1 417 777 3787
e-mail: ajlewis@kpmg.ca

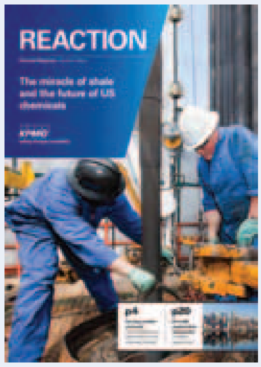
Global COO
Paul Harnick
Tel: +1 215 407 1911
e-mail: paulharnick@kpmg.com

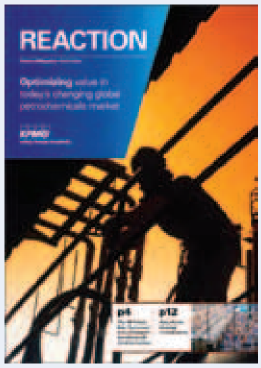
Read the latest edition of Reaction Magazine on your iPad anytime, anywhere.
To learn more visit, **kpmg.com/ipad**

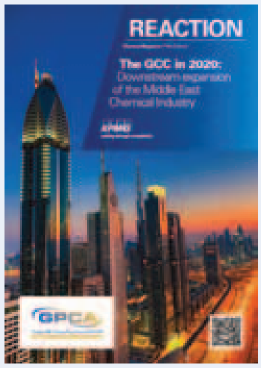
kpmg.com/chemicals

Designed by Evalueserve.
Global Program Delivery by Meghan Bested
Publication name: Reaction Magazine – Eighth Edition
Publication number: 120995
Publication date: September 2012

Missed an issue of Reaction?







Back issues are available to download from: **www.kpmg.com/reaction**

kpmg.com/socialmedia